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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

No. 323

INSULAR SUGAR REFINING CORPORATION,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

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INSULAR SUGAR REFINING CORPORATION,
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v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

Insular Sugar Refining Corporation prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit, entered in the above entitled cause on June 11, 1945, affirming in part a decision of the Tax Court of the United States.

Statement of the Matter Involved

The Circuit Court of Appeals, *by a divided Court,* affirmed a decision of the Tax Court, holding certain "drawbacks" of processing taxes subject to unjust enrichment tax and deciding that the burden was on the petitioner to show that it had not passed on these taxes.

Statutes

The Statutory provisions involved, Section 17(a) of the Agricultural Adjustment Act and Section 501(b) of the Revenue Act of 1936, are set forth in the Appendix at pages 15 and 17, respectively.

Question Presented

Were "drawbacks," paid to an exporter pursuant to the Agricultural Adjustment Act, subject to unjust enrichment tax?

Reasons for the Allowance of the Writ

1. The Circuit Court of Appeals for the Second Circuit has decided a Federal question in a way probably in conflict with the applicable decisions of this Court. In *Campbell, et al.* v. *U. S.*, 107 U. S. 407, and the cases which follow it, this Court decided that "drawbacks" are provided by Congress to exempt exports from taxation, and when the taxed article is exported, the United States becomes bound to pay the drawback to the exporter. The decision of the Court below interpreting the applicable statutory provisions as requiring the imposition of an 80% unjust enrichment tax on such "drawbacks" cannot be reconciled with those decisions.

2. The decision of the Court below is in conflict with the decision of the Circuit Court of Appeals for the Seventh Circuit in *Cudahy Bros.* v. *LaBudde*, 92 F. (2d) 937 (certiorari denied, U. S. 303, 659). In that case it was pointed out that Section 17(a) of the Agricultural Adjustment Act was re-enacted by Congress as part of the Revenue Act of 1936 with the intent to preserve the exemption

of exports from tax and to confirm the authority of the Commissioner of Internal Revenue to continue paying the "drawbacks" pursuant to that section after the Agricultural Adjustment Act was held unconstitutional. *Contrary to the decision of the Court below,* the Court in that case held that this legislative intent precluded a construction of the Revenue Act which would make "drawbacks" under Section 17(a) subject to the provisions of the Revenue Act applicable to refunds of taxes illegally collected, requiring that a claimant prove that he had not passed on the tax, etc.

WHEREFORE, this petitioner prays that a writ of certiorari be issued directed to the U. S. Circuit Court of Appeals of the Second Circuit, requiring that this cause be certified to this Court for review and determination of all errors assigned.

INSULAR SUGAR REFINING CORPORATION

By J. STERLING HALSTEAD

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I. Opinion of the Court Below

The official report of the opinion of the U. S. Circuit Court of Appeals for the Second Circuit in this proceeding has not yet been published.

II. Jurisdiction

This Court has jurisdiction to review the judgment below under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (U. S. C. A. Title 28, Section 347, 42 Stat. 938).

III. Statutes and Regulations Involved

The Statutes and Regulations involved are set forth in the Appendix *infra,* pages 15 to 23, inclusive.

IV. Statement of the Case

The Petitioner, Insular Sugar Refining Corporation, during the years involved in this proceeding was engaged in refining sugar in the Philippine Islands (R. 30) and selling about 90% of its production in the United States through Balfour, Guthrie & Co., Limited of San Francisco (R. 31-32).

Petitioner customarily purchased in the United States containers for its sugar, burlap cotton lined and cotton bags, through its parent Company and its agent, Balfour, Guthrie & Co., Limited (R. 31).

Bags purchased to be used as containers for sugar sold in the Philippine Islands were marked by the manufacturer with brand name "Suchar." Bags purchased for

sugar to be imported and sold in the United States were marked with the brand names "Snowflake" and "Quick-melt" (R. 62).

During the year 1935, Petitioner purchased and exported 1,201,028 such bags to its refinery in the Philippines (R. 53, 90; Pet. Ex. A). Cotton processing taxes had been paid on these bags by the manufacturer, Pacific Diamond H. Bag Company (R. 31, 50). When the bags were exported, the manufacturer filed claims and in 1936 collected "drawbacks" totaling $6,358.68 (R. 32), as agent for Petitioner (R. 148).

Later the Respondent mailed to Petitioner a 90-day letter claiming an "unjust enrichment tax" on these drawbacks (R. 9). This proceeding resulted.

V. Specification of Errors

The Circuit Court of Appeals erred:

1. In holding "drawbacks" paid under Section 17(a) of the Agricultural Adjustment Act subject to unjust enrichment tax;

2. In deciding that petitioner was not entitled to exemption from unjust enrichment tax under Section 501(b) of the Revenue Act of 1936;

3. In concluding that the applicable statutory provisions required, as a condition to exemption from unjust enrichment tax, that petitioner prove that it had not passed on the tax refunded to it in the form of drawbacks.

VI. Summary of Argument

The majority of the Circuit Court of Appeals, in sustaining the 80% tax on the "drawbacks" received by the Petitioner, have reached a result in conflict with the pur-

pose of the Congress in providing for "drawbacks" and contrary to its intent in imposing an unjust enrichment tax. In denying exemption to Petitioner they have placed a construction on the statutory provisions involved which is unnecessary and erroneous.

ARGUMENT

POINT I

The imposition of an unjust enrichment tax on "drawbacks" is inconsistent with the intent of the Congress in providing for the payment of drawbacks and contrary to its expressed intent in enacting the Unjust Enrichment Tax Law.

The "drawbacks" of processing tax, on which the Respondent here seeks to impose an unjust enrichment tax, were allowed under Section 17(a) of the Agricultural Adjustment Act (Title 7, Chapter 26, Sec. 617(a), U. S. C. A.), because the bags on which this processing tax had been paid, were exported to the Philippine Islands. This statute provided:

> "*Upon the exportation to* any foreign country (and/or to *the Philippine Islands,* the Virgin Islands, American Samoa, the Canal Zone, and the island of Guam) *of any product* processed wholly or partly from a commodity *with respect to which product* or commodity *a tax had been paid* or is payable under this chapter, *the tax due and payable or due and paid shall be credited or refunded* • • •.
>
> Under regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, a credit or refund shall be allowed to the consignor named in the bill of lading under which the product is exported or to the shipper or to the person liable for the tax provided

the consignor waives any claim thereto in favor of such shipper or person liable for the tax." (Italics supplied.)

(Re-enacted by Section 601 of the Revenue Act of 1936 and amended to apply only to refunds on goods exported before January 1, 1936.)

The purpose of such drawbacks is to exempt exports from tax. In *Campbell, et al.* v. *United States*, 107 U. S. 407, this Court said at page 413:

> "The purpose of the drawback provision is to make duty-free, imports which are manufactured here and then returned whence they came or to some other foreign country."

On the basis of this legislative intent to make exports tax-free, rights created by Section 17(a) of the Agricultural Adjustment Act as re-enacted by Section 601(a) of the Revenue Act of 1936 have been held exempt from the other provisions of that Act relating to taxes illegally assessed and collected. *Cudahy Bros.* v. *LaBudde*, 92 F. (2d) 937, C. C. A. 7th Cir. In that case the Court said at page 938:

> "It will be observed that originally Congress, by section 17 (48 Stat. 40), with the obvious intent of stimulating exportation and foreign trade and to relieve the country of an undesirable domestic surplus, placed exported goods in an exempt class, against which no tax was intended to be assessed or collected. It went even further and provided that one exporting commodities might, upon giving bond to the Secretary of the Treasury, process the commodity and export same without payment of any tax. That exported goods were exempt and that Congress intended by the exemption to encourage exportation is evidenced by the further provision of the section that any tax paid should be refunded to the consignor so exporting and to no other person, except at the direction of the consignor. This provision was similar to other so-called 'drawback'

statutes, one of which was before the Supreme Court in *Asiatic Petroleum Co.* v. *Insular Collector,* 297 U. S. 666, 56 S. Ct. 651, 80 L. Ed. 967, where the purpose of exemption was commented upon, and another in *Campbell et al.* v. *United States,* 107 U. S. 407, 2 S. Ct. 759, 763, 27 L. Ed. 592, where the Court remarked that when Congress declared that upon exportation a 'drawback' of the duty paid, should be allowed, there 'resulted a contract that when exported the government would refund, repay, pay back, this amount as a drawback to the importer.' Thus, we observe, appellee sought to recover no taxes collected under an invalid statute *but rather refund of taxes previously paid, upon proof that the commodity taxed had gone into exportation.*"

• • • • • • •

(p. 939)

"We conclude that Congress, by its reenactment of section 17, recognized the cause of action and the established remedy therefor; that *to place the consignor of exported goods declared by law to be exempt from taxation in the same category with processors who are suing to recover taxes illegally collected under an invalid act of Congress and to require them to conform to a procedure which is inapplicable to their situation* and the details of which, under the regulations of the commissioner, are wholly inapplicable to the facts in the case of exportation, *is to do violence to the intent of Congress.* We believe that Congress has not rescinded its obvious intent to exempt exported goods from taxation, but rather, that its intent was to protect in good faith those persons whom it induced to make exportation under an act providing for such exemption and by re-enactment of section 17(a) to recognize the obligation to perform the government's contract with such exporting consignors." (Italics supplied.)

Contrary to this decision of the Circuit Court of Appeals for the Seventh Circuit holding such procedure "wholly inapplicable" to drawbacks, both the Tax Court

and the majority of the Court below erroneously decided that this Petitioner must prove that it had "not passed on the processing tax" which was the subject of the "drawback."

The intent of the Congress that such drawbacks should be exempt from unjust enrichment tax appears clearly in the report of the Senate Finance Committee, *Senate Report No. 2156,* pages 25-26, where the Committee in discussing the Unjust Enrichment Tax Law stated:

> "The principal amendments proposed by your Committee are as follows: • • •
>
> "(2) There is excluded from the computation of unjust enrichment the income relating to transactions of such character that the non-payment or recovery of the amount of the excise tax can be assumed not to have constituted a windfall. These cases are enumerated in Section 501(b) (explained below) • • •:
>
> "§ 501(b)—This is a new provision. It excludes from the computation of income resulting in unjust enrichment • • • *any income from which articles with respect to which some statutory provision for refund existed, as in the case of exports,* charitable deliveries, etc." (Italics supplied.)

POINT II

Petitioner is entitled to exemption under Section 501(b) of the Unjust Enrichment Tax Law.

(a) The statutory provision imposing the unjust enrichment tax specifically exempts repayments to taxpayers entitled to the refund otherwise than as an illegal collection.

Section 501(b) of the Revenue Act of 1936 provides:

> "(b) The net income • • • shall not include the net income • • • from Federal excise tax with respect to any article,

"* * * (3) If, under the terms of any statute the taxpayer would have been entitled to a refund from the United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection * * *."

"(j) (5) The term 'taxpayer' means a person subject to a tax imposed by this section."

(b) Petitioner comes within the exempt class.

Section 501(b)(3) makes the exemption applicable "if *under the terms of any statute,* the taxpayer *would have been* entitled to a refund * * * of the Federal Excise Tax * * *."

It defines taxpayer as "a person subject to a tax imposed by this section (the unjust enrichment tax).

Under Regulations 83, Art. 3 (App., p. 15), promulgated by the Respondent, either the consignor or "the person for whom the consignor * * * is handling the product for shipment" was authorized to file a claim for drawback pursuant to Section 17(a) of the Agricultural Adjustment Act.

Pacific Diamond H. Bag Company, the consignor, was "handling the bags for Petitioner."

The bags subjected to processing tax in this case became the property of the Petitioner prior to the time of export (a) because they were unconditionally appropriated to Petitioner by Diamond H. Pacific Bag Company when the brand names were printed on the bags, under which Petitioner's sugar was sold (Netherton Dep. 24-25), and (b) because they were delivered to the carrier by Diamond H. Pacific Bag Company "for the purpose of transmission" to Petitioner (R. 145).

California Civil Code, Dir. III, Part 4, Title 1, Chapter 2, Article 1, Section 1739 (*Hillyers Consolidated Supplement to the California Code 1927-1931,* Part 1, p. 5538), provides:

> "Rule 4. 1. *Where there is a contract to sell unascertained or future goods by description and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer, or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer.* Such assent may be expressed or implied and may be given either before or after the appropriation is made.
>
> "2. Where, in pursuance of a contract to sell, the seller delivers the goods to the buyer, or to a carrier or other bailee (whether named by the buyer or not) for the purpose of transmission to or holding for the buyer, he is presumed to have unconditionally appropriated the goods to the contract." (Italics supplied.)

As the bags became the property of the Petitioner before they were exported, in delivering the bags to the carrier, Diamond H. Pacific Bag Company was "handling" the bags for the Petitioner. Under *Regulations 83, Article 3, supra,* petitioner was, therefore, the shipper and entitled to exemption under Section 501(b)(3) as one who "**would have been entitled to a refund** from the United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection * * *."

The decision of the majority of the Court below, however, denies the exemption because

> "the actual consignor had not waived its right to claim the refund—as required by statute—but had actually made such claim and received the refund" (R. 145).

This view ignores the fact that in drafting Section 501(b) Congress used the words "if under the terms of any statute the taxpayer *would have been entitled to a refund*" and interprets it as if Congress had said instead that a taxpayer should only be entitled to the exemption

if it "has claimed and *received a refund* * * *." The language of Section 501(b), *supra,* as enacted, obviously was not intended to restrict the exemption to cases where taxpayer itself had filed a claim based on some ground other than illegal or erroneous collection and on the basis of that claim had received the refund in question.

If the right to such a refund existed, the refund is exempt no matter how the taxpayer obtained the repayment in issue.

As Judge HINCKS pointed out in his dissenting opinion below (R. 147):

> "The use of the past subjunctive 'would have been entitled' clearly imports a contrary to the fact condition which, since not expressed, must be implied. And plainly the condition to be implied is in substance the situation and the legal relationships which existed after the exportation had been accomplished and Insular had paid the processing tax to its vendor Diamond *and before Diamond had collected a refund of the tax from the government.*" (Italics supplied.)
>
> * * * * * * *
>
> (R. 148)
>
> "To be sure, to perfect a claim for refund in its own name as shipper—which it was—Insular would have needed among other things Diamond's waiver. But there is utterly nothing in the record to suggest that Diamond, which had already acknowledged Insular's beneficial interest in the refund, would not have cooperated to that end by voluntarily furnishing the necessary waiver of its right as consignor. And if it had objected, the relationship of the parties was such that Insular could have compelled the execution of the necessary waiver. Thus viewed, in the situation which the statute envisaged Insular 'would have been entitled' to the refund and to any waiver by Diamond necessary to effectuate the refund."

The right to a refund under any Federal revenue statute is subject to various conditions. Among other requirements, the taxpayer must file a claim before the expiration of the Statute of Limitations, and that claim must contain the basis for recovery on which any later suit for a refund is brought. Obviously, it cannot have been intended by the Congress that in order that a taxpayer be entitled to exemption under Section 501(b) it must show that it has complied with all these conditions. The words *"would have been entitled"* negatives such a construction.

In order to be entitled to exemption under this Section it is only necessary that a taxpayer show that it had rights which, if enforced, would have resulted in its receiving the refunds in question. The fact that it did not enforce these rights or go through the required procedure is immaterial in so far as the application of this exemption provision is concerned. **The existence of the rights determined the exempt status.**

This construction of the statute in question, as Judge HINCKS has concluded in his dissenting opinion, is (R. 149):

> "wholly consistent with the applicable Revenue Act and the Agricultural Adjustment Act. Yet it gives effect to the clear Congressional intent, just referred to, to save our foreign trade from the dampening effect of the processing tax,—an objective which is frustrated if the proceeds of the drawbacks are subjected to the windfall tax."

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

J. STERLING HALSTEAD,
Counsel for Petitioner,
Insular Sugar Refining Corporation.

APPENDIX

"Reg. 83, Art. 3. (As amended by T. D. 4671, dated July 27, 1936.) CLAIM FOR REFUND.—(a) (1) *Who may file claim.*—A. The consignor named in the bill of lading under which the product is exported shall be entitled to make claim for refund unless he shall have waived such right to the shipper. *Consignor named in the bill of lading* means the person named in the bill of lading as the person from whom the carrier received the product for shipment.

"B. The shipper, if other than the consignor named in the bill of lading, shall be entitled to make claim for the refund only if the consignor shall have waived any claim to such refund to him. *In such case, the term shipper means the person for whom the consignor named in the bill of lading is handling the product for shipment.*" (Italics supplied.)

U. S. CODE ANNOTATED, CHAPTER 26, TITLE 7, 49 STAT. 1739

§ 617. REFUND ON GOODS EXPORTED: BOND TO SUSPEND TAX ON COMMODITY INTENDED FOR EXPORT.

(a) Upon the exportation to any foreign country (and/or to the Philippine Islands, the Virgin Islands, American Samoa, the Canal Zone, and the island of Guam) of any product processed wholly or partly from a commodity with respect to which product or commodity a tax has been paid or is payable under this chapter, the tax due and payable or due and paid shall be credited or refunded. Under regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, the credit or refund shall be allowed to the consignor named in the bill of lading under which the product

is exported or to the shipper or to the person liable for the tax provided the consignor waives any claim thereto in favor of such shipper or person liable for the tax. In the case of rice, a tax due under this title which has been paid by a tax-payment warrant shall be deemed for the purpose of this subsection to have been paid; and with respect to any refund authorized under this section, the amount scheduled by the Commissioner of Internal Revenue for refunding shall be paid, any provision of law notwithstanding. In the case of sugar beets and sugarcane, this subsection shall be applicable to exports of products thereof to the Philippine Islands, the Virgin Islands, American Samoa, the Canal Zone, and/or the island of Guam only if this chapter with respect to sugar beets and sugarcane is not made applicable thereto. The term "product" includes any product exported as merchandise, or as a container for merchandise, or otherwise.

(b) Upon the giving of bond satisfactory to the Secretary of the Treasury for the faithful observance of the provisions of this chapter requiring the payment of taxes, any person shall be entitled, without payment of the tax, to process for such exportation any commodity with respect to which a tax is imposed by this chapter or to hold for such exportation any article processed wholly or partly therefrom. May 12, 1933, c. 25, Title I, § 17, 48 Stat. 40; May 9, 1934, 11:23 a.m., c. 263, §§ 12, 13, 48 Stat. 676; Mar. 18, 1935, c. 32, § 11, 49 Stat. 48; Aug. 24, 1935, c. 641, § 28, 49 Stat. 770; June 22, 1936, 9:00 p.m., c. 690, § 601, 49 Stat. 1739.

REVENUE ACT OF 1936, C. 690, 49 STAT. 1648

TITLE III—TAX ON UNJUST ENRICHMENT

SEC. 501. TAX ON NET INCOME FROM CERTAIN SOURCES.

(a) The following taxes shall be levied, collected, and paid for each taxable year (in addition to any other tax on net income), upon the net income of every person which arises from the sources specified below:

(1) A tax equal to 80 per centum of that portion of the net income from the sale of articles with respect to which a Federal excise tax was imposed on such person but not paid which is attributable to shifting to others to any extent the burden of such Federal excise tax and which does not exceed such person's net income for the entire taxable year from the sale of articles with respect to which such Federal excise tax was imposed.

(2) A tax equal to 80 per centum of the net income from reimbursement received by such person from his vendors of amounts representing Federal excise-tax burdens included in prices paid by such person to such vendors, to the extent that such net income does not exceed the amount of such Federal excise-tax burden which such person in turn shifted to his vendees.

(3) A tax equal to 80 per centum of the net income from refunds or credits to such person from the United States of Federal excise taxes erroneously or illegally collected with respect to any articles, to the extent that such net income does not exceed the amount of the burden of such Federal excise taxes with respect to such articles which such person shifted to others.

(b) The net income (specified in subsection (a) (1)) from the sale of articles with respect to which the Federal

excise tax was not paid, and the net income specified in subsection (a) (2) or (3), shall not include the net income from the sale of any article, from reimbursement with respect to any article, or from refund or credit of Federal excise tax with respect to any article (1) if such article (or the articles processed therefrom) were not sold by the taxpayer on or before the date of the termination of the Federal excise tax; (2) if the taxpayer made a tax adjustment with respect to such article (or the articles processed therefrom) with his vendee; or (3) if under the terms of any statute the taxpayer would have been entitled to a refund from the United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection (assuming, in case the tax was not paid, that it had been paid).

(c) The net income from the sales specified in subsection (a) (1) shall be computed as follows:

(1) From the gross income from such sales there shall be deducted the allocable portion of the deductions from gross income for the taxable year which are allowable under the applicable Revenue Act; or

(2) If the taxpayer so elects by filing his return on such basis, the total net income for the taxable year from the sale of all articles with respect to which each Federal excise tax was imposed (computed by deducting from the gross income from such sales the allocable portion of the deductions from gross income which are allowable under the applicable Revenue Act, but without deduction of the amount of such Federal excise tax which was paid or of the amount of reimbursement to purchasers with respect to such Federal excise tax) shall be divided by the total quantity of such articles sold during the taxable year and the quotient shall be multiplied by the quantity of such articles involved in the sales specified in subsection (a) (1). Such quantities shall be expressed in terms of the unit on the basis of which the Federal excise tax was imposed.

For the purposes of this section the proper apportionment and allocation of deductions with respect to gross income shall be determined under rules and regulations prescribed by the Commissioner with the approval of the Secretary.

(d) The net income from reimbursement or refunds specified in subsection (a) (2) or (3) shall be computed as follows: From the total payment or accrual (1) of reimbursement to the taxpayer from vendors for amounts representing Federal excise tax burdens included in prices paid by the taxpayer to such vendors or (2) of refunds or credits to the taxpayer of Federal excise taxes erroneously or illegally collected, there shall be deducted the expenses and fees reasonably incurred in obtaining such reimbursement or refunds.

(e) For the purposes of subsection (a) (1), (2), and (3), the extent to which the taxpayer shifted to others the burden of a Federal excise tax shall be presumed to be an amount computed as follows:

(1) From the selling price of the articles there shall be deducted the sum of (A) the cost of such articles plus (B) the average margin with respect to the quantity involved; or

(2) If the taxpayer so elects by filing his return on such basis, from the aggregate selling price of all articles with respect to which such Federal excise tax was imposed and which were sold by him during the taxable year (computed without deduction of reimbursement to purchasers with respect to such Federal excise tax) there shall be deducted the aggregate cost of such articles, and the difference shall be reduced to a margin per unit in terms of the basis on which the Federal excise tax was imposed. The excess of such margin per unit over the average margin (computed for the same unit) shall be multiplied by the number of such units represented by the articles with respect to which the computation is being made; but

(3) In no case shall the extent to which the taxpayer shifted to others the burden of the Federal excise tax with respect to the articles be deemed to exceed the amount of such tax with respect to such articles minus (A) the portion of the amount of the Federal excise tax (or of the reimbursement specified in subsection (a) (2)) with respect to the articles which is paid or credited by the taxpayer to any purchasers as specified in subsection (f) (3) and minus (B) the amount of any increase in the tax under section 602 of the Revenue Act of 1932 for which the taxpayer under this section became liable as the result of the nonpayment or refund of the Federal excise tax with respect to the articles.

(f) As used in this section—

(1) The term "margin" means the difference between the selling price of articles and the cost thereof, and the term "average margin" means the average difference between the selling price and the cost of similar articles sold by the taxpayer during his six taxable years preceding the initial imposition of the Federal excise tax in question, except that if during any part of such six-year period the taxpayer was not in business, or if his records for any part of such period are so inadequate as not to furnish satisfactory data, the average margin of the taxpayer for such part of such period shall, when necessary for a fair comparison, be deemed to be the average margin, as determined by the Commissioner, of representative concerns engaged in a similar business and similarly circumstanced.

(2) The term "cost" means, in the case of articles manufactured or produced by the taxpayer, the cost to the taxpayer of materials entering into the articles; or, in the case of articles purchased by the taxpayer for resale, the price paid by him for such articles (reduced in both cases by the amount for which he is reimbursed by his vendor).

(3) The term "selling price" means selling price minus (A) amounts subsequently paid or credited to the purchaser on or before June 1, 1936, or thereafter in the bona fide settlement of a written agreement entered into on or before March 3, 1936, as reimbursement for the amount included in such price on account of a Federal excise tax; and minus (B) the allocable portion of any professional fees and expenses of litigation incurred in securing the refund or preventing the collection of the Federal excise tax, not to exceed 10 per centum of the amount of such tax.

(g) In determining costs, selling prices, and net income, the taxpayer shall, unless otherwise shown, be deemed to have sold articles in the order in which they were manufactured, produced, or acquired. Where the taxpayer's records do not adequately establish the quantity of a commodity taxable under the Agricultural Adjustment Act, as amended, entering into articles sold by him, such quantities shall be computed by the use of the conversion factors prescribed in regulations under such Act, as amended.

(h) If the taxpayer made any purchase or sale otherwise than through an arm's-length transaction, and at a price other than the fair market price, the Commissioner may determine the purchase or sale price to be that for which such purchases or sales were at that time made in the ordinary course of trade.

(i) Either the taxpayer or the Commissioner may rebut the presumption established by subsection (e) by proof of the actual extent to which the taxpayer shifted to others the burden of the Federal excise tax. Such proof may include, but shall not be limited to:

(1) Proof that the change or lack of change in the margin was due to changes in factors other than the tax. Such factors shall include any clearly shown change (A) in the type or grade of article or materials, or (B) in costs of production. If the taxpayer asserts that the burden of the

tax was borne by him while the burden of any other increased cost was shifted to others, the Commissioner shall determine, from the respective effective dates of the tax and of the other increase in cost as compared with the date of the change in margin, and from the general experience of the industry, whether the tax or the increase in other cost was shifted to others. If the Commissioner determines that the change in margin was due in part to the tax and in part to the increase in other costs, he shall apportion the change in margin between them.

(2) Proof that the taxpayer modified contracts of sale, or adopted a new contract of sale, to reflect the initiation, termination, or change in amount of the Federal excise tax, or at any such time changed the sale price of the article (including the effect of a change in size, package, discount terms, or any other merchandising practice) by substantially the amount of the tax or change therein, or at any time billed the tax as a separate item to any vendee or indicated by any writing that the sale price included the amount of the tax, or contracted to refund any part of the sale price in the event of recovery of the tax or decision of its invalidity; but the taxpayer may establish that such acts were caused by factors other than the tax, or that they do not represent his practice during the period in which the articles in question were sold.

(j) As used in this section—

(1) The term "Federal excise tax" means a tax or exaction with respect to the sale, lease, manufacture, production, processing, ginning, importation, transportation, refining, recovery, or holding for sale or other disposition, of commodities or articles, provided for by any Federal statute, whether valid or invalid, if denominated by a "tax" by such statute. A Federal excise tax shall be deemed to have been imposed with respect to an article if it was imposed with respect to (or with respect to the processing

of) any commodity or other article, from which such article was processed.

(2) The term "date of the termination of the Federal excise tax" means, in the case of a Federal excise tax held invalid by a decision of the Supreme Court, the date of such decision.

(3) The term "refund or credit" does not include a refund or credit made in accordance with the provisions and limitations set forth in Title VII of this Act, or in section 621 (d) of the Revenue Act of 1932.

(4) The term "tax adjustment" means a repayment or credit by the taxpayer to his vendee of an amount equal to the Federal excise tax with respect to an article (less reasonable expense to the vendor in connection with the nonpayment or recovery by him of the amount of such tax and in connection with the making of such repayment or credit) if such repayment or credit is made on or before June 1, 1936, or thereafter in the bona fide settlement of a written agreement entered into on or before March 3, 1936.

(5) The term "taxpayer" means a person subject to a tax imposed by this section.

(k) All references in this section to the purchase or sale (or to parties to the sale) of articles with respect to which a Federal excise tax was imposed shall be deemed to include the purchase or sale (or parties to the sale) of services with respect to which a Federal excise tax was imposed, and for the purposes of subsection (a) the extent to which the taxpayer shifted to others the burden of such Federal excise tax with respect to such services shall be presumed to be an amount computed as follows: From the selling price of the services there shall be deducted the average price received by the taxpayer for performing similar services during the six taxable years preceding the initial imposition of the Federal excise tax in question. The

balance (to the extent that it does not exceed the amount of such Federal excise tax with respect to such services minus any payments or credits with respect to the services made to purchasers as specified in subsection (f) (3)) shall be the extent to which the taxpayer shifted the burden of such Federal excise tax to others. If during any part of such six-year period the taxpayer was not in business, or if his records for any part of such period are so inadequate as not to furnish satisfactory data, the average price of the taxpayer for such part of such period shall, when necessary for a fair comparison, be deemed to be the average price, as determined by the Commissioner, of representative concerns engaged in a similar business and similarly circumstanced. The presumption established by this subsection may be rebutted by proof of the character described in subsection (i).

(l) The taxes imposed by subsection (a) shall be imposed on the net income from the sources specified therein, regardless of any loss arising from the other transactions of the taxpayer, and regardless of whether the taxpayer had a taxable net income (under the income-tax provisions of the applicable Revenue Act) for the taxable year as a whole; except that if such application of the tax imposed by subsection (a) is held invalid, the tax under subsection (a) shall apply to that portion of the taxpayer's entire net income for the taxable year which is attributable to the net income from the sources specified in such subsection.

SEC. 503. ADMINISTRATIVE PROVISIONS.

(a) All provisions of law (including penalties) applicable with respect to taxes imposed by Title I of this Act, shall, insofar as not inconsistent with this title, be applicable with respect to the taxes imposed by this title, except that the provisions of sections 101, 131, 251, and 252 shall not be applicable.

(b) Every person (1) upon whom a Federal excise tax was imposed but not paid, or (2) who received any reimbursement specified in subsection (a) (2), or (3) who received a refund or credit of Federal excise tax, shall make a return under this title, which return shall contain such information and be made in such manner as the Commissioner, with the approval of the Secretary, shall prescribe.

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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 323

INSULAR SUGAR REFINING CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 29–39) are reported in 3 T. C. 922. The opinion and dissenting opinion of the Circuit Court of Appeals (R. 142–149) are unreported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 27, 1945 (R. 149–150). The petition for a writ of certiorari was filed on August 14, 1945. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Was the taxpayer subject to the unjust enrichment tax imposed by Section 501 (a) (2) of the Revenue Act of 1936 on the amount of $6,358.68 reimbursed to it by its vendor during the fiscal years ended November 30, 1935, and November 30, 1936, on account of processing tax included in the price of cotton bags purchased by the taxpayer where the taxpayer failed to prove that it bore the burden of the tax?

2. Is the taxpayer exempt from the unjust enrichment tax under the provisions of Section 501 (b) of the Revenue Act of 1936?

STATUTE AND REGULATIONS INVOLVED

The applicable provisions of the statute and regulations are set out in the Appendix, *infra*, pp. 13–15.

STATEMENT

The facts as found by the Tax Court (R. 30–33) may be summarized as follows:

This proceeding involves deficiencies in unjust enrichment tax for the taxable fiscal years ended November 30, 1935, and November 30, 1936 (R. 29).

The taxpayer, referred to as Insular, is a corporation, organized under the laws of the Philippine Islands with its principal office in Manila, and is engaged in refining sugar. During the years in question it was a subsidiary of the International Sugar Corporation, a New York cor-

poration, referred to as "Suchar." The taxpayer's Pacific Coast agent in this country was Balfour, Guthrie & Company, Ltd., called "Balfour." (R. 30.)

In keeping with trade custom, the taxpayer's sugar was packed and sold in containers holding 100 pounds of sugar each.[1] About 90 percent of it was exported to the United States and sold by Balfour. The balance was sold in the Philippines. The containers used were purchased in the United States by Suchar for the taxpayer's account or through Balfour. They were exported to the taxpayer and all but those used in the Philippine trade were filled with sugar and subsequently exported. During the periods here involved, Balfour, acting as purchasing agent for the taxpayer, ordered various amounts of bags from Pacific Diamond H Bag Company, called "Diamond." Diamond shipped the bags to the taxpayer at Manila prior to January 6, 1936, and appeared as consignor in the shipping papers. The prices charged taxpayer for such bags included cotton processing taxes totalling

[1] An export container consisted either of a burlap bag with a cotton liner or a burlap bale containing ten to twenty small cotton bags called "pockets." The containers used in the Philippine trade were single large cotton bags. The cost of the bags fluctuated but averaged, less tax, about 12 cents each for the single large bags, 14 cents for burlap bags with cotton liners and 24 cents or 29 cents for the bales of pockets. The sales price of sugar also fluctuated but not in relation to price changes in bags. (R.31.)

$6,358.68 which Diamond had borne. Coincident with the issuing of invoices covering the several purchases, credit memoranda were made and sent to taxpayer showing the amount of refund which would be payable to taxpayer as and when the tax was refunded to Diamond by the Government.[2] (R. 31.)

Claims for refund of the cotton processing tax were filed by Diamond and allowed in the sum of $6,358.68 and reimbursement thereof was made by Diamond to the taxpayer. The taxpayer incurred no expense in connection with these reimbursements. (R. 32.) The cotton processing tax went into effect on August 1, 1933. The tax amounted to about nine-tenths of a cent on a large bag and two and two-tenths cents on a bale of pockets. The taxpayer's sale price was increased from $4.50 to $4.60 per 100 pounds of sugar on August 1, 1933. (R. 32.) When shipments of bags were made to it, the taxpayer set up a debit memorandum on its books in the approximate amount of

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[2] This was pursuant to a circular letter mailed on June 25, 1934, by Diamond to its customers stating that all its bills and contracts would carry the following clause (R. 32):

"Cost of cotton cloth, of which bags herein invoiced (sold) are composed, includes processing tax paid by manufacturer of said cloth. In the event it is determined that on any bags herein referred to, seller is entitled to refund of all or any part of such tax, and when and if payment of such refund is received by seller, the amount of such payment received will be remitted to the buyer."

the tax included in the price of the bags. This item was treated as an asset and was cancelled when the reimbursement was received. Neither taxpayer nor Suchar instructed Balfour to add the cotton processing tax to the sales price of sugar. (R. 33.)

The Commissioner held that unjust enrichment taxes were due under the provisions of Section 501 (a) (2) of the Revenue Act of 1936, upon the reimbursements received by the taxpayer from Diamond on account of cotton processing taxes (R. 29). The Tax Court sustained the action of the Commissioner (R. 40) and the Circuit Court of Appeals affirmed (R. 149),[3] one judge dissenting (R. 147–149).

ARGUMENT

1. By Section 501 (a) (2) (Appendix, *infra*, p. 13) of Title III of the Revenue Act of 1936 Congress imposed an unjust enrichment tax equal to 80 percent of the net income from reimbursement received by a vendee from his vendor of amounts representing the federal excise tax burden included in the price paid by the vendee to his vendor to the extent that the vendee shifted the tax burden to others in any manner.

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[3] The case was remanded to the Tax Court to determine the exact amount of reimbursement received in the fiscal years ending November 30, 1935, and November 30, 1936, respectively (R. 146–147).

The primary purpose of the Act[4] was to tax profits realized in the form of a refund of processing taxes (as a result of the decision in *United States* v. *Butler*, 297 U. S. 1, declaring the Agricultural Adjustment Act, c. 25, 48 Stat. 31, as amended, unconstitutional) in cases where the taxpayer had shifted or passed the tax on to its vendees.

Insular admittedly received reimbursement of $6,358.68 from its vendor, Diamond, representing cotton processing tax paid by Insular to Diamond which had been included in the price of cotton bags purchased by Insular from Diamond. The Tax Court held (R. 36–39) that Insular failed to establish it bore the burden of the tax and had not shifted it to sugar purchasers. The evidence showed (R. 32, 37) on the date the cotton processing tax went into effect, August 1, 1933, the taxpayer raised the price of its sugar 10 cents per

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[4] H. Rep. No. 2475, 74th Cong., 2d Sess., p. 11 (1939–1 Cum. Bull. (Part 2) 667, 675) states:

"Where the taxpayer is a person who bought articles at a price including the burden of the excise and resold them at a price also including the burden of the excise, there shall be computed the net income attributable to any reimbursement he receives from his vendor for the burden of the excise, and this amount (limited by the extent to which he shifted the burden of the excise to his customers) is subject to the tax."

See also S. Rep. No. 2156, 74th Cong., 2d Sess., pp. 24–27 (1939–1 Cum. Bull. (Part 2) 678, 694–696).

100 pounds, which was sufficient to pass on the burden of the tax and more.[5] The question of whether or not the tax burden had been shifted was one of fact for determination of the Tax Court, and the Circuit Court of Appeals (R. 146) accepted the Tax Court's finding as binding.

On this record Insular has failed completely to establish that it bore the burden of the cotton processing tax, and since it has received reimbursement from its vendor for the taxes paid by it, it is liable for the unjust enrichment tax imposed by Section 501 (a) (2) of the Revenue Act of 1936.

2. To avoid the unjust enrichment tax Insular claims exemption under Section 501 (b) (3) of the Revenue Act of 1936 (Appendix, *infra,* pp. 13–14) and necessarily relies upon Section 17 (a) of the Agricultural Adjustment Act, as amended by the Act of August 24, 1935, c. 641, 49 Stat. 750, Section 28, and as reenacted by Section 601 (a) of the Revenue Act of 1936 for the limited purpose of allowing refunds thereunder where the exportation, as here, took place prior to January 6, 1936. *Wilson & Co.* v. *United States,*

[5] Unjust enrichment tax returns on Form 945 for the years ended November 30, 1935, and November 30, 1936, were filed with the Collector but these returns did not contain marginal computations permitted by Section 501 (e) of the Revenue Act of 1936 (Appendix, *infra,* pp. 14–15) to establish presumptions as to the shifting of the tax burden to others (R. 30–31).

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311 U. S. 104. The statute reads, in part, as follows:

> SEC. 17 (a). Upon the exportation * * * to the Philippine Islands * * * of any product processed wholly or partly from a commodity with respect to which product or commodity a tax has been paid * * * under this title, the tax * * * due and paid shall be * * * refunded. Under regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, the credit or refund shall be allowed to the consignor named in the bill of lading under which the product is exported or to the shipper or to the person liable for the tax provided the consignor waives any claim thereto in favor of such shipper or person liable for the tax. * * * (7 U. S. C., Sec. 617.)

It will be observed that the statute states in specific and unequivocal terms that the refund upon exportation of the taxed article is to be allowed (1) to the consignor or, (2) if the consignor waives his claim in favor of the shipper, to the shipper or (3) if the consignor waives his claim in favor of the person liable for the tax, to such person.

The Tax Court (R. 36) and the Circuit Court of Appeals (R. 144–146) held that Insular was not one who could claim a refund under Section 17 (a) of the Agricultural Adjustment Act. It was not the consignor under the shipping papers

but was the consignee. Insular urges (Pet. 11–12) that it was the shipper on the ground that the bags had been appropriated to its use prior to their exportation. But here again Diamond was the actual shipper. Even assuming *arguendo* that Insular was the shipper, there is still no showing that Diamond waived its claim for refund in its favor as required by the express terms of the statute. In fact Diamond itself claimed and obtained the refund from the Government. Thus Insular was not entitled to a refund under the specific terms of the statute and the exemption provided for in Section 501 (b) is not available to it.

Treasury Regulations[6] relied upon by Insular (Pet. 11) merely confirm the Government's position that the consignor is the person entitled in the first instance to file a claim for refund. He may waive that right in favor of the shipper but until he does so his right to the refund is paramount. But there was no such waiver in the instant case, for Diamond filed the claim and received the refund from the Government. Diamond was not Insular's agent. There is no proof that it was handling the bags for the taxpayer. It was selling bags to Insular through Insular's agent, Balfour.

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[6] Article 3, Regulations 83, as amended by T. D. 4671, XV–2 Cum. Bull. 424, 427 (1936). (See Appendix, *infra*, p. 15.)

In short, Insular was neither consignor nor shipper and cannot bring its case within the purview of the exemption statute.

3. There is no conflict of decisions as asserted by the taxpayer (Pet. 2). The repeated characterization by Insular of this reimbursement to it of cotton processing taxes by the vendor, Diamond, as a "drawback" is a misnomer and erroneous.

Thus *Campbell* v. *United States,* 107 U. S. 407, 411, is not in point. That case held that a person entitled by statute to a drawback may, after payment is refused by the Treasury, maintain a suit in the Court of Claims on the basis of an implied contract. But even if that case were applied to the facts of the instant case, any implied contract to repay was between Diamond, the exporter, and the Government and not between Insular and the Government. Moreover, subsequent to the *Campbell* case, it has been made plain that an export refund is not a contract right but a gratuity. *Swan & Finch Co.* v. *United States,* 190 U. S. 143, 146; *cf. United States* v. *Allen,* 163 U. S. 499.

The case of *Cudahy Bros. Co.* v. *La Budde,* 92 F. 2d 937 (C. C. A. 7th),[7] certiorari denied, 303 U. S. 659, does not deal with a question arising under Section 501 (b) of the Revenue Act of

[7] It should be noted that the *Cudahy* decision is doubtful authority in view of *Wilson & Co.* v. *United States,* 311 U. S. 104.

1936 (cf. Pet. 2, 8–9). The plaintiff there was the processor, consignor and exporter of the exported articles and the issue was whether it could recover the export refund without complying with the requirements of Title VII of the Revenue Act of 1936 relating to the refund of amounts collected under the Agricultural Adjustment Act. As pointed out above, Insular was neither the processor, consignor nor exporter. It was merely a purchaser of cotton bags to the price of which the vendor, Diamond, had added the processing tax and on refund being made to Diamond, it, in turn, reimbursed Insular.

The taxpayer relied below upon the decision in *Helvering* v. *Insular Sugar Refining Corp.*, 141 F. 2d 713 (App. D. C.), and urged that since the court there held the taxpayer absorbed $.2244 per bag of the processing tax on sugar sold, it must also have absorbed the cotton processing tax on bags (Br. 15). That conclusion by no means follows and the decision is not *res judicata* of the question here because the tax on sugar and on cotton are separate and distinct taxes. That case cannot supplement the proof in the instant case since the Tax Court has found the taxpayer failed to prove that the cotton processing tax on bags was not shifted to its customers (R. 32, 37–39). *Cf. Insular Sugar Refining Corp.* v. *United States*, 49 F. Supp. 319 (C. Cls.).

CONCLUSION

There is no conflict of decisions and the decisions below are correct. The petition should be denied.

Respectfully submitted.

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SEPTEMBER 1945.

APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

TITLE III—TAX ON UNJUST ENRICHMENT

SEC. 501. TAX ON NET INCOME FROM CERTAIN SOURCES.

(a) The following taxes shall be levied, collected, and paid for each taxable year (in addition to any other tax on net income), upon the net income of every person which arises from the sources specified below:

* * * * *

(2) A tax equal to 80 per centum of the net income from reimbursement received by such person from his vendors of amounts representing Federal excise-tax burdens included in prices paid by such person to such vendors, to the extent that such net income does not exceed the amount of such Federal excise-tax burden which such person in turn shifted to his vendees.

* * * * *

(b) The net income (specified in subsection (a) (1)) from the sale of articles with respect to which the Federal excise tax was not paid, and the net income specified in subsection (a) (2) or (3), shall not include the net income from the sale of any article, from reimbursement with respect to any article, or from refund or credit of Federal excise tax with respect to any article * * * (3) if under the terms of any statute the taxpayer would have been entitled to a refund from the

United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection (assuming, in case the tax was not paid, that it had been paid).

* * * * *

(e) For the purposes of subsection (a) (1), (2), and (3), the extent to which the taxpayer shifted to others the burden of a Federal excise tax shall be presumed to be an amount computed as follows:

(1) From the selling price of the articles there shall be deducted the sum of (A) the cost of such articles plus (B) the average margin with respect to the quantity involved; or

(2) If the taxpayer so elects by filing his return on such basis, from the aggregate selling price of all articles with respect to which such Federal excise tax was imposed and which were sold by him during the taxable year (computed without deduction of reimbursement to purchasers with respect to such Federal excise tax) there shall be deducted the aggregate cost of such articles, and the difference shall be reduced to a margin per unit in terms of the basis on which the Federal excise tax was imposed. The excess of such margin per unit over the average margin (computed for the same unit) shall be multiplied by the number of such units represented by the articles with respect to which the computation is being made; but

(3) In no case shall the extent to which the taxpayer shifted to others the burden of the Federal excise tax with respect to the articles be deemed to exceed the amount of such tax with respect to such articles minus (A) the portion of the amount of the

Federal excise tax (or of the reimbursement specified in subsection (a) (2)) with respect to the articles which is paid or credited by the taxpayer to any purchasers as specified in subsection (f) (3) and minus (B) the amount of any increase in the tax under section 602 of the Revenue Act of 1932 for which the taxpayer under this section became liable as the result of the nonpayment or refund of the Federal excise tax with respect to the articles.

Article 3, Treasury Regulations 83, as amended by T. D. 4671, XV—2 Cum. Bull. 424, 427 (1936) provides:

Claim for Refund.—(a) (1) *Who may file claim.*—A. The *consignor* named in the bill of lading under which the product is exported shall be entitled to make claim for refund unless he shall have waived such right to the shipper. *Consignor named in the bill of lading* means the person named in the bill of lading as the person from whom the carrier received the product for shipment.

B. The *shipper*, if other than the consignor named in the bill of lading, shall be entitled to make claim for the refund only if the consignor shall have waived any claim to such refund to him. In such case, the term *shipper* means the person for whom the consignor named in the bill of lading is handling the product for shipment.

* * * * *

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